United States Court of Appeals

for the Second Circuit

APPELLANT'S PETITION FOR REHEARING

75-7538

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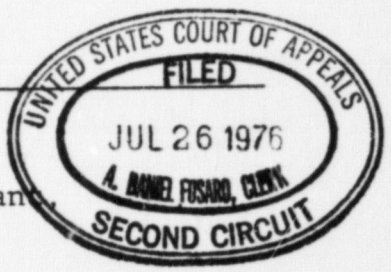
FOR THE SECOND CIRCUIT



ALAN L. SPIELMAN,

Plaintiff-Appellant,

- against -

GENERAL HOST CORPORATION, RICHARD C. PISTELL, HARRIS J. ASHTON, C. WHITCOMB ALDEN, JR., JOSEPH P. BINNS, WILLIAM F. DOWNEY, WESTON E. HAMILTON, WILLIAM P. HOWE, JR., J. ELROY McCAW, EDWIN C. McDONALD, LESLIE W. SCOTT, ALLEN & CO., INC., ALLEN & CO., KLEINER, BELL & CO., INC., SEYMOUR M. LAZAR, EUGENE V. KLEIN, ALLEN MANUS, CECIL MANUS and GREAT AMERICAN INSURANCE COMPANY,

Defendants,

GENERAL HOST CORPORATION, RICHARD C. PISTELL, HARRIS J. ASHTON, C. WHITCOMB ALDEN, JR., JOSEPH P. BINNS, WESTON E. HAMILTON, LESLIE W. SCOTT, ALLEN & CO., INC., and ALLEN & CO.,

Defendants-Appellees.

B P/S

APPELLANT'S PETITION FOR REHEARING AND SUGGESTION OF REHEARING EN BANC

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

ALAN L. SPIELMAN, Plaintiff-Appellant, - against - GENERAL HOST CORPORATION, RICHARD C. PISTELL, HARRIS J. ASHTON, C. WHITCOMB ALDEN, JR., JOSEPH P. BINNS, WILLIAM F. DOWNEY, WESTON E. HAMILTON, WILLIAM P. HOWE, JR., J. ELROY McCAW, EDWIN C. MCDONALD, LESLIE W. SCOTT, ALLEN & CO., INC., ALLEN & CO., KLEINER, BELL & CO., INC., SEYMOUR M. LAZAR, EUGENE V. KLEIN, ALLEN MANUS, CECIL MANUS and GREAT AMERICAN INSURANCE COMPANY, Defendants, GENERAL HOST CORPORATION, RICHARD C. PISTELL, HARRIS J. ASHTON, C. WHITCOMB ALDEN, JR., JOSEPH P. BINNS, WESTON E. HAMILTON, LESLIE W. SCOTT, ALLEN & CO., INC., and ALLEN & CO., Defendants-Appellees.	Docket No. 75-7538

APPELLANT'S PETITION FOR REHEARING
AND SUGGESTION OF REHEARING EN BANC

TO THE HONORABLE, THE JUDGES OF
THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT:

Pursuant to Rules 35 and 40 of the Federal Rules of Appellate Procedure, Appellant petitions for rehearing and suggests the appropriateness of rehearing en banc of this Court's decision of July 12, 1976, affirming the judgment of the District Court in favor of the defendants.

General Host Corporation ("General Host") and Greyhound Corporation ("Greyhound") sought to acquire Armour Corporation ("Armour") by way of

competing exchange and tender offers for Armour convertible debentures and common stock. Greyhound offered cash. General Host, whose net worth was approximately $37.5 million (J.A. 855) offered a package consisting of $347 million of debentures to be issued, together with 14 million warrants to purchase common stock of General Host. At the conclusion of the competing offers, General Host obtained approximately 55% ownership of Armour and Greyhound obtained approximately 32%.

General Host was unable to obtain operating control of Armour, notwithstanding its 55% interest. Accordingly, General Host was unable to utilize Armour's immense assets to satisfy General Host's debt requirements, including debt service to be incurred with respect to the $347 million of debentures. Thereafter, within five months of the conclusion of the exchange offer, General Host was forced to contract to sell its 55% of Armour to Greyhound, sustaining a loss in excess of $50 million and causing a substantial decline in the value of the debentures and warrants issued by General Host to the Armour security holders who tendered their Armour convertible debentures and common stock to General Host.

At the trial, heard non-jury by the District Court, plaintiff, representing a class of Armour common stock and convertible debenture holders (J.A. 583)[1/] who accepted the General Host tender, alleged that

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1/ The class was defined by stipulation and order of the lower court as including

> "(B) Those persons or entities who purchased or otherwise acquired Armour and Company securities, either common stock or convertible debentures, between July 29, 1968 and February 14, 1969, did not accept The Greyhound Corporation tender offer, and exchanged said Armour and Company securities for General Host Corporation debentures and warrants issued pursuant to the said Exchange Offer;"

the General Host exchange prospectus was materially misleading in that it gave assurances to the class members that General Host, if it achieved more than 50% ownership of Armour, would control Armour and then could utilize Armour's assets to help satisfy General Host's debt requirements, including those to be incurred with respect to the interest payments on the $347 million of debentures. The Trial Court refused to sustain plaintiff's contention that the Prospectus was materially misleading, and further concluded that other information made available to the class members sufficiently informed them of the risks that ultimately caused their losses.

This Court found that, contrary to the finding of the Trial Court, the General Host Prospectus conveyed:

> "...'the misleading impression' that General Host '...would be able to satisfy its cash flow requirements out of the target company (Armour & Co.) assets, implying as it did that General Host would gain operating control of Armour as a result of the exchange offer and that operating control would permit General Host to increase Armour's dividends and sell Armour's assets, thereby benefiting General Host.'" Slip. Op. pp. 4861. 2/

The Court further recognized the materiality of the control issue.3/

2/ Actually there was a two-fold misleading impression created by this assertion of General Host, (a) that General Host would gain immediate operating control of Armour and (b) that as a result thereof it would be legally permitted to make use of Armour's assets for its own benefit.

3/ "The necessity for obtaining operating control was to provide cash flow to meet, inter alia, interest requirements on the offeror's substantial indebtedness, including but not limited to its debentures issued in exchange for the target company's stock." Id., n. 3.

Nevertheless, this Court affirmed the judgment of the District Court in favor of the defendants, on the ground that "the 'total mix' of communications to, and presumptive knowledge of, 'shareholders' of the target company renders harmless a potentially misleading omission in the prospectus circulated by the tender offeror.'" Slip Op., p. 4861.

In evaluating the "total mix", this Court placed special emphasis on a proxy statement sent to shareholders of Armour, soliciting their votes for directors. This proxy statement was mailed to Armour stockholders two weeks before the effective date of the General Host Prospectus, and a supplement thereto was mailed to Armour stockholders four days before the expiration of the tender offer. The Court reasoned that:

> "In taking the affirmative act of voting, shareholders were likely to take special notice of these facts [staggered board and cumulative voting]". Slip Op. p. 4863.

Plaintiff respectfully submits that this Court erred in the following particulars, warranting a rehearing and reversal of its decision.

1. The aforesaid Armour Proxy Statements were sent only to holders of Armour common stock as of January 7, 1969. They were not sent to holders of Armour convertible debentures or to persons who acquired Armour common stock after January 7, 1969, which groups are also included in the class. Thus, there is no basis in the record for concluding that statements in the proxy materials rendered harmless the misleading statements and omissions in the prospectus as to these two groups of class members.

2. In the case of all class members, the Court correctly perceived that: "Generally, the 'total mix' would be insufficient to

compensate for omissions in the prospectus since an investor is all too apt to look upon those communications as self-serving and to consider the prospectus as a more objective, self-contained statement upon which he may justifiably rely to make an informed investment decision." Slip Op., p. 4863. The Court erred when it concluded that this salutary principle should be disregarded because the target company had a staggered board and cumulative voting, facts of which its own stockholders were "presumably aware". The record lacked any evidence that they were actually aware of those facts, or, more importantly, aware of their legal consequences in preventing General Host from assuming operating control of Armour. The Court's reliance on a presumption of knowledge to defeat the policy of full and truthful disclosure basic to the Securities Exchange Act[4/] involves questions of exceptional importance, justifying a rehearing en banc.

I

The "Total Mix" and Presumptive Awareness Do Not Apply to Armour's Debenture Holders and Post January 7, 1969 Shareholders

The class on whose behalf this case was tried comprised both Armour shareholders and Armour debenture holders to whom the General Host prospectus was addressed and who exchanged their Armour securities for General Host warrants and debentures. 402 F.Supp. at 192-193.

4/ Section 10(b), U.S.C. §78j(b), and Rule 10b-5, and Section 14(e) of the Williams Act, 15 U.S.C. §8n(e).

In applying the "total mix" analysis to neutralize the materially misleading impression created by the General Host prospectus, this Court time and again referred to communications to Armour shareholders regarding their own corporation's staggered board and cumulative voting, particularly the proxy statement and supplement thereto, sent by the Armour management to its shareholders "within two weeks of the effective date of the prospectus, and again four days before expiration of the tender offer." Those materials were addressed to the Armour shareholders of record as at January 7, 1969 only. (J.A. 658, 692 (A-29), 1089). They were not sent to the debenture holders or the post January 7th shareholders.[5/] Nor is there any evidence in the record that the letters addressed and mailed to Armour stockholders on January 9, 1969 and February 10, 1969 were mailed to debenture holders (Stipulation 32 and 36, J.A. 657 and 658.) In the case of those class members, therefore, the "total mix" analysis is inapplicable, and the decision of the District Court, rather than being "unassailable", is without support.

II

The "Total Mix" Defense Should Not Be Applied In The Absence Of Actual Evidence That The Class Members Were In Fact Aware Of Both The Existence And Consequences Of Armour's Staggered Board And Cumulative Voting

There is no evidence in the record that the class members actually

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5/ These class members had no voting rights at the Armour February 21, 1969 Annual Meeting and therefore were not among those who "[i]n taking the affirmative act of voting,...were likely to take special notice of these [staggered board and cumulative voting] facts."

knew the consequences of the Armour staggered board and cumulative voting. In holding that the misleading prospectus was rendered harmless, the Court has relied entirely on the presumed knowledge of its recipients. In so holding, the Court has lost sight of the controlling principle that "...the 1934 Act and its companion legislative enactments embrace a 'fundamental purpose...to substitute a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the securities industry'...." Affiliated Ute Citizens of Utah v. United States, 406 U.S. 128, 92 S.Ct. 1456, 1471 (1972).

It has been held that "...[i]n light of the Supreme Court's holding in Affiliated Ute, the burden of proof rests squarely upon defendant to establish the 'non-reliance' of plaintiff." Rochez Bros., Inc. v. Rhoades, 491 F.2d 402, 410 (3d Cir. 1974). Analogously, defendants relying on a "total mix" defense should not be permitted to prevail on the basis of presumptions which are at odds with reality. If the defense is available, evidence of actual knowledge should be required to sustain it. Cf. Blackie v. Barrack, 524 F.2d 891, 906 (9th Cir. 1975).

As previously noted, this Court soundly concluded that: "Generally, the 'total mix' would be insufficient to compensate for omissions in the prospectus since an investor is all too apt to look upon those communications as self-serving and to consider the prospectus as a more objective, self-contained statement upon which he may justifiably rely to make an informed investment decision."

By contrast, there is no sound reason to suppose that shareholders receiving Armour proxy materials, while considering whether or not to tender to General Host, would be able to make a sophisticated analysis of the implications of Armour's staggered board and cumulative voting and relate it to what they were being told in the General Host prospectus. The probability is that they would have paid no attention to the proxy materials for election of Armour directors especially since the Annual Meeting was scheduled to take place after the tender. The class members all tendered to General Host and thereafter had no further interest in Armour's Annual Meeting.

In TSC Industries, Inc. v. Northway, Inc., 96 S.Ct. 2126, 2133 (1976), decided after the argument in this case, the Supreme Court, dealing with the standard of materiality under proxy provisions of the Securities Exchange Act, concluded that "...there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[6/] There can be no doubt that if the prospectus here had adequately spelled out the obstacles to General Host's taking operating

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6/ The Court also noted: "...to the extent that the existence of control was, at the time of the proxy statement's issuance, a matter of doubt to those responsible for preparing the statement, we would be unwilling to resolve that doubt against facts so obviously suggestive of control." Id., n. 15. Here, it is the converse, the absence of control, which mandated full and fair disclosure.

control of Armour, the "total mix" would have been significantly altered.

Rather than relying on an unrealistic presumption of knowledge to defeat the fundamental purpose of the Securities Exchange Act mandating full disclosure

> "to achieve a high standard of business ethics in the securities industries", p. 6, supra, this Court should apply the principle well established in the related field of the law of trusts, that "for a cestui que trust to 'ratify' or confirm a breach of trust, he must be apprised of all the material facts and as well of their legal effect. No half-hearted disclosure or partial discovery is sufficient in either respect. The trustee's duty of disclosure is not discharged by leaving the cestui to draw doubtful inferences, conclusions and suspicions from his efforts to extract for his own benefit not only the trust res but other property or the beneficiary as well. Plaintiff's suspicions did not constitute the full knowledge of all the material facts upon which confirmation may be predicated. Furthermore, he obviously had no conception of the legal significance of those facts." Earll v. Picken, 113 F.2d 150, 158 (D.C.Cir. 1940). (Emphasis added)

So here, in light of the broad, remedial purposes of the Securities Exchange Act of 1934 it is regressive for this Court to establish a precedent that shareholders cannot rely on representations in an Exchange Offer Prospectus. Instead, they are held to a standard of caveat emptor, requiring them to disregard General Host's representations, in a situation where there is no evidence that they knew the existence of the staggered board and cumulative voting provisions, let alone the consequences of those provisions.

CONCLUSION

For the reasons stated, Appellant requests that his petition for rehearing be granted and suggests the appropriateness of rehearing en banc.

Dated: July 26, 1976

Respectfully submitted,

MILBERG & WEISS

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STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

LINDA S. BAKER being duly sworn, deposes and says that she is in the employ of Milberg & Weiss, attorneys for the within named Plaintiff herein, and is over the age of 21 years. That on the 26 day of July, 1976, she served the within Plaintiff's Petition for Rehearing and Suggestion for Rehearing En Banc upon the attorneys for the respective parties named below, by depositing two copies of same to each of them, securely enclosed in postpaid wrappers in a post office box regularly maintained by the United States Government at One Pennsylvania Plaza, New York, New York, directed to each of them at their respective addresses set forth below, those being the addresses within the State designated by them for that purpose on the preceding papers in this action, or the places where they then kept their respective offices between which places there then was and now is a regular communication by mail:

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Attys for Defendant-Appellee
Allen & Co., Inc.

Linda S. Baker

Sworn to before me this
26th day of July, 1976.

Mae Eisenberg
Notary Public

MAE EISENBERG
Notary Public, State of New York
No. 30-4606174 Qual. in Nassau Co.
Cert. Filed in New York County
Commission Expires March 30, 1977